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## Electricity sector restructuring in Belgium during the 90's

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### Abstract

Since 1925, the Belgian liberal statutory framework, combined with weak supervision by public authorities, allowed the Tractebel conglomerate and its subsidiary Electrabel to strengthen in the nineties their dominant position in all parts of the Belgian electricity market. The implementation of the EU internal market of electricity directive speeded up the process of market liberalisation. However, the urgency of the law-giving process and the traditionally overwhelming power of the incumbent interests of the Tractebel conglomerate will bring about a merely formalistic opening of the Belgian electricity market. © 2000 Published by Elsevier Science Ltd. All rights reserved.

*Keywords:* Deregulation; Competition; Electricity; Belgium

### 1. Introduction

Over the last 10 years the Belgian electricity supply sector has been significantly restructured reducing the number of independent players. While in 1989 there were four generators, their number went down to two in 1999. Since early 1988 there has been a continuous shift of ownership and control positions resulting in the only private generator since 1990, Electrabel, a subsidiary of the Tractebel holding, to be indirectly controlled by the French holding company, Suez–Lyonnaise des Eaux. The 1995 convention between Electrabel and the public generators in SPE has completed the strengthening of the private Belgian generator in the forthcoming European energy market. Electrabel–SPE generates 96% of Belgian electricity and both control the network operator CPTE. In spring 1996 Electrabel also reinforced its power at the retail supply level by concluding long-term agreements with the municipal boards having stakes in the mixed intermunicipal utilities. The latter cover 80% of the retail power market.

Due to Electrabel's de facto private monopoly in the

electricity market, liberalisation in Belgium depended upon European proposals leading to the adoption of EU-directive 96/92. In June 1998 the Belgian government started the process of implementation. Early in 1999 the electricity bill was drawn up and approved by the Chamber and Senate in March and April respectively, resulting in the adoption of the Electricity Act on April 29.

This paper<sup>1</sup> describes the restructuring process of the Belgian electricity sector in the 90s. The necessary implementation of EU-directive 96/92 presented a unique opportunity to set up a legal framework establishing a real competitive electricity sector. However, the weakness of the European directive, the quite different initial structures of the industry in the member states, as well as the attitudes of some governments towards the restructuring process may have set back this opportunity. The final outcome remains to be seen. In Belgium, the extreme urgency of the reform process and the strong interests of Tractebel have been weighing on the liberalisation process.

In Section 2 we depict the background to the restructuring process paying attention to the legal and institutional energy framework, and the financial and industrial structure of the energy sector. Section 3 focuses on the preparation of the new legal and regulatory elec-

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<sup>1</sup> The opinions expressed in this paper are purely personal.

tricity framework and critically assesses the main issues covered by the new Electricity Act.

The study of the legal and institutional framework begins with the liberal 1925 Electricity Supply Act, and offers a concise survey of other statutory instruments relating to the energy sector. With regard to public policy, public authorities being favourable to regulation by convention were willing to give up their regulatory and supervisory powers over the electricity market participants. This was formalised in the 1955 agreement concluded by the social partners founding the Control Committee for Electricity (CCE) and renamed CCEG in 1964 when the gas sector was added. At the financial level, the attempted take-over raid in January 1988 on the Société Générale de Belgique, Belgium's major holding company, announced a decade of shuffling stakes ultimately resulting in the Belgian electricity sector being directly and indirectly controlled by the French utility holding, Suez-Lyonnaise des Eaux. At the industrial level, Electrabel and SPE concluded the 1995 convention aiming at co-operation in generation and transmission. In spring 1996 Electrabel completed its vertically integrating strategy by renewing prematurely the existing distribution/retail supply contracts with municipal boards that participate in the mixed intermunicipal utilities.

The second part concerns the new Electricity Act. The several documents and stages in the legislative process are discussed. Special attention is given to the hearing in the Commission for Economic Affairs and in particular to the remarks of the invited speakers. The main issues of electricity liberalisation are then discussed and critically commented on. Those encompass regulation, an independent network operator, generation planning, investment and licensing for new construction plans, network access and eligibility, price regulation, unbundling, public service obligations and stranded costs.

## 2. Background to electricity restructuring in Belgium

### 2.1. Legal framework

Belgian institutions are characterised by a complicated system of agreements and rules emanating from intertwined organisations in the absence of a clearly developed statutory framework. Energy is no exception. This is due to three related factors. Firstly, public authorities<sup>2</sup> generally believed that energy issues were best taken care of by the Tractebel conglomerate, controlling most of the power sector in Belgium. Secondly, inde-

pendent think tanks on energy policy in Belgium are weak<sup>3</sup>, and no public utility commission was created to get a firm grip on the sector. Thirdly, the reform of Belgium from a centralised state towards a federal nation has scattered competencies among the different public authorities.

The liberal Electricity Supply Act of 10 March 1925 constituted the basic legal foundation for electricity supply. Electricity generation is neither regulated by exclusive rights nor subject to the grant of a licence. Every natural person or legal person has the right to generate electricity to meet their own demand and the right to deliver electricity to natural and legal persons. Likewise, the municipalities and provinces may generate and deliver power to their constituencies. Access to the transmission grid is not provided for by any statutory provision. However, permits for rights-of-way for the construction of transmission lines are granted by regional authorities. No statutory provision requires the unbundling of generation and distribution activities.

The 1925 Act assigns municipalities the monopoly rights on electricity distribution for supplies up to 1000 kW. Supply to customers with a maximum demand in excess of 1000 kW is subject to competition. Every municipality or association of municipalities may grant a supply licence to a natural or legal person. As distribution of electricity became a regional competence under the state reforms, the Walloon region altered the threshold to 10 000 kW by Decree of 2 November 1990. De facto are in the Flemish region customers with a demand not exceeding 4000 kW supplied by intermunicipal utilities. Municipalities decide autonomously how to organise their distribution monopoly. They can exercise their exclusive right individually or join with other municipalities in so-called intermunicipal utilities. The interest of the municipalities in intermunicipal utilities is confirmed by the Act of 22 December 1986.

There are two types of intermunicipal utilities. When there is no private company involved, the public organisation carries out all the distribution related tasks. Those are referred to as pure or public intermunicipal utilities (PIU). When a private company participates in an intermunicipal utility, the former takes care of the management and daily operation. They form mixed intermunicipal utilities (MIU). There are 19 MIU providing about 80% of electricity distribution and 9 PIU supplying the remaining 20%. Electrabel, the private generator, owns at least 50% of the MIU share capital.

The Act of 12 April 1965 concerns transport of gaseous and similar products by means of pipelines. Gas transport for provisioning the public distribution is sub-

<sup>2</sup> Confirmed by oral statements from the former Minister-President of Flanders, Luc Vandenbrande, and the former Belgian Prime Minister, Jean-Luc Dehaene.

<sup>3</sup> Compared to independent Energy Research Centres abroad, the few institutions consulted by federal and regional governments — for instance STEM, CES, VITO and Institut Wallon — are extremely weak.

jected to a public service licence. Gas transport for other purposes requires a ministerial permit. Although there is no specific statutory provision on gas distribution, municipalities deliver gas via PIU and MIU to households and small industrial consumers, based on their monopoly on rights of ways for gas distribution.

The reform of the Belgian state took place in successive waves. National legislative and executive powers were attributed to three regions, Flanders, Wallonia and Brussels, and to three communities, the Flemish Community, the French Community and the German-speaking Community. Regions have powers in the field of energy policy. Each region and community has its own government and parliament. National legislative acts no longer have precedence over regional and community acts. Conflicts have to be decided by the Arbitration Court. Implementation of EU-directives can take place not only at the national level but also at the regional level.

According to the Act of 8 August 1980 regional authority on electricity supply remained in charge of electricity distribution through low-voltage networks not exceeding 30 kV. The Act also required ESI investment plans in power generation and high-voltage transmission to be advised by the National Committee on Energy (NCE). The exclusive licence for import, export, transport and storage of gas was conferred upon Distrigas, by that time a mixed company with a public majority and with private partners, Shell, Exxon and Intercom. However, the Act of 29 July 1983 limited the exclusive licence to underground storage and transport of gas. Distrigas ensures the permanent coverage of 100% of the total need for public distribution.

Statutory provision 6 VII of the Act of 8 August 1988 strongly reinforced the regional competencies. With regard to electricity and gas, the regional aspects now comprise: distribution and local transport of electricity via low-voltage networks not exceeding 70 kV, public gas distribution, renewable energy sources, energy recovery and energy conservation. Four areas requiring technical and economic indivisibility remain under federal authority: investment planning; nuclear fuel cycle; infrastructures of storage, transport and generation of energy; and tariffs. By Act of 6 July 1993 Belgium officially has become a federal state.

## *2.2. Formal regulation since 1955 covers the absence of public policy in the electricity sector*

Instead of developing regulatory powers, public authorities have left the initiative for supervision of the power sector to the private sector itself. The recession of 1952–53 and the lack of any governmental initiative to lower electricity prices encouraged the socialist trade union to demand the nationalisation of the electricity sector at a special congress held in October 1954. The

employers' federation adhering to a system of freedom under state control reacted to the socialist request by inviting the trade unions and electricity companies to start negotiations that ended with the electricity peace treaty of 1955, as well as the founding of the Control Committee for Electricity (CCE). In 1964 its supervising authority was extended to the gas sector, at that time renamed the Control Committee for Electricity and Gas (CCEG). CCEG is responsible for price control in the power sector, save for prices charged to the largest electricity consumers.

This new form of regulation by convention resulted from an agreement between social partners. The agreement itself as well as the CCEG is thus the result of a private negotiation process that was started and completed by the employers' and employees' federations. The political authorities supported the negotiation process fully and were willing to give up the sovereignty of governing the power sector by regulation or by nationalising the entire or central parts of the electricity supply sector. Since that period the federal government in Belgium has been very cautious concerning interventions in the power sector. In practice, most interventions were negotiated in advance with the members of the CCEG.

The main objectives of the 1955 agreement were "to realise a further rationalisation of the sector, to pursue a more co-ordinated and unified management (now BCEO–CGEE), in order to lower the price of electricity". To reach these objectives, the CCEG brings out unanimous recommendations. Generally, the CCEG has an unchallenged authority and all players obey its recommendations. Although the charter founding the National Committee on Energy (NCE) in 1975 endowed the latter with comprehensive supervision of the energy sector, it has not been very active as it lacked the necessary scientific staff to perform this task. The main and almost only activity NCE pursued was the organisation of hearings about the power sector investment plans.

By Royal Order NR. 147 of 30 December 1982, the CCEG was institutionalised and transformed into an organ of public utility having a maximum of authority. Currently, CCEG is composed of three organs having a different status. The "controlling organs" comprise the Federation of Belgian Enterprises (FBE) and the three main labour trade unions. Unfortunately, one of the most influential members of FBE is the electricity and gas sector and so the electricity generators can put pressure on the FBE-representative. The "controlled organs" are, at the generation and transport level, BCEO–CGEE and Gas CTD and, at the distribution level, Intermixt and Inter-Regies, representing the MIU and PIU. The "observing organs" are representatives of the federal and regional governments.

Since the renewal of the CCEG agreement in spring 1995, the tariff recommendations have become binding

by ministerial order. The federal government also has the right to suspend CCEG recommendations involving energy policy or those affecting consumers. The regional governments have the same rights and competencies in matters entrusted to them by the state reforms. However, the governments' participation is of minor importance as they lack any voting power. In practice the CCEG is a prototype of the "captured regulator", acting in the interests of incumbents of the industry rather than in the interests of consumers or potential entrants to the industry. Its secretariat is fully financed by the energy sector and housed in the Electrabel headquarters. So far the secretariat has not shown the ability to generate its own ideas, but has merely depended on the think-thank of the Tractebel group. The separation of power between the government, employers' federations and trade unions serves to undermine certain parliamentary democracy as they form a limited part of the whole society, act in the interests of incumbents of the industry and have installed a system of self-control by electricity generators and distributors.

### 2.3. A decade (1988–1998) of shifting ownership and control positions

Up to September 1987 the shareholding structure of the Société Générale de Belgique (SGB) was largely disseminated among the public. At the extraordinary General Meeting of 7 September 1987 it appeared that a dozen of mainly French companies had acquired about 20% of the SGB share capital. To dilute the possible participation of a hostile shareholder one proceeded to a double increase of capital, also authorising the board of directors to increase the share capital. On 17 January 1988 the Italian tycoon Carlo De Benedetti informed CEO Lamy that his group was holding 18.6% of SGB's shares and intended to launch a public offer bid bringing the group's participation to 33.6%. Accordingly, the board of directors decided to increase the capital for subscription by a subsidiary. This gave rise to legal disputes due to the poor state of Belgian legislation concerning public offer bids and the purchase by companies or their subsidiaries of the former's shares (Fig. 1).

In February 1988 Suez announced its 10% stake in SGB. From that moment on there were two camps fighting for control over SGB. Already two months later it appeared that 55% was in the hands of several Belgian, Luxembourg and Swiss shareholders and the Suez group, of which the latter had 28%. The remaining 45% was held by the Group De Benedetti. At the end of June 1988 the two groups reached a compromise consisting of a reduction of De Benedetti's stake to 16% in exchange for a reinforcement of the latter's stake in Suez. By December 1988 Suez acquired the majority position leading to a 60% stake by February 1991.

The SGB–Group Bruxelles Lambert (GBL) energy

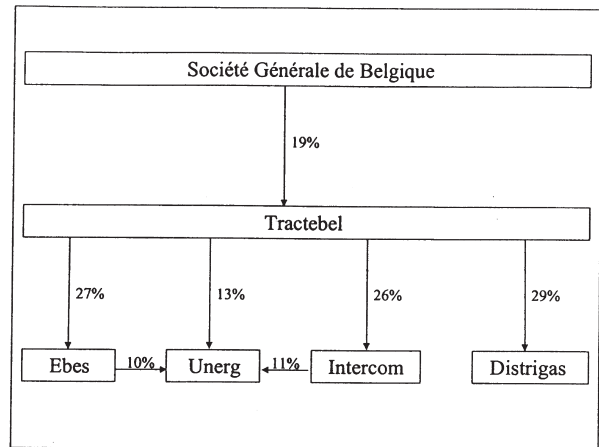


Fig. 1. Control structure of the Belgian energy sector (January 1988).

pact was signed in March 1989. The financier Albert Frère heads GBL. Following this pact SGB acquired 39% of the shares in Tractebel, GBL obtained 26%. Tractebel was the result of the 1986 merger between the holdings Tractionel and Electrobel. Tractebel is composed of three divisions: engineering and industry, energy and telecommunication. Tractebel plays a pivotal role in Belgium's energy supply via its controlling interests in Electrabel and Distrigas, which dominate the country's power and gas sectors respectively. Until March 1999, the central management position was held by Mr. Philippe Bodson. CEO Bodson came from the very competitive glass industry.

In July 1990 Tractebel, being the major shareholder in the three private generators Ebés (30%), Unerg (37%) and Intercom (30%), regrouped its activities in Electrabel and created Powerfin for investment in electricity and gas assets abroad. Through these operations Tractebel's indirect and direct control over Electrabel amounted to 42% and over Powerfin to 64% (Fig. 2). Compared to 1988, Tractebel's share in Distrigas, the gas transport and storage company, increased to 33.25%.

In spring 1994 the Belgian government decided to sell out its 50% share in Distrigas. Until then Distrigas share capital was 50% publicly and 50% privately owned. Tractebel (33.25%) and Belgian Shell (16.67%) were the private shareholders. After privatisation Distrigas share capital was divided as follows. The PIU and MIU concluded an agreement for acquiring 16.62% of the shares via Publigas. Publigas has 50% – 1 share in Distrihold. The remaining 50% + 1 share is held by Tractebel. Distrihold has 16.75% of the Distrigas' shares. This means that the municipalities now have about 25% (16.62% + almost  $\frac{1}{2}$  of Distrihold). Tractebel's direct and indirect participation now equals 41.6%. Belgian Shell retained its participation and the rest is floated on the Stock Exchange (Fig. 3).

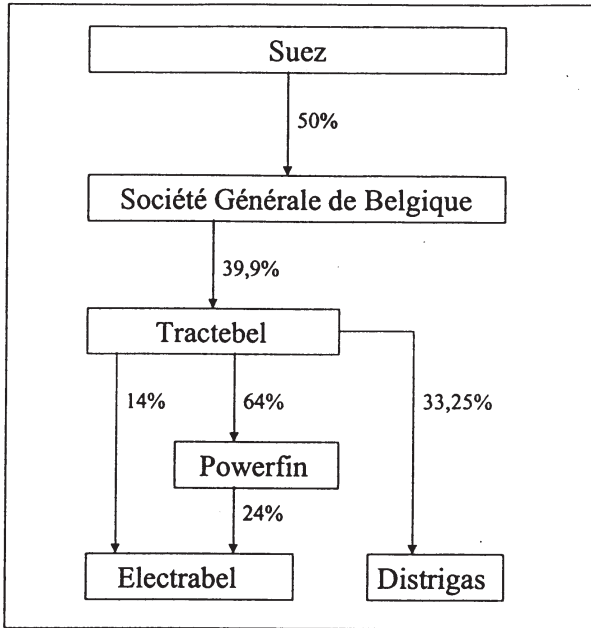


Fig. 2. Control structure of the Belgian energy sector (July 1990).

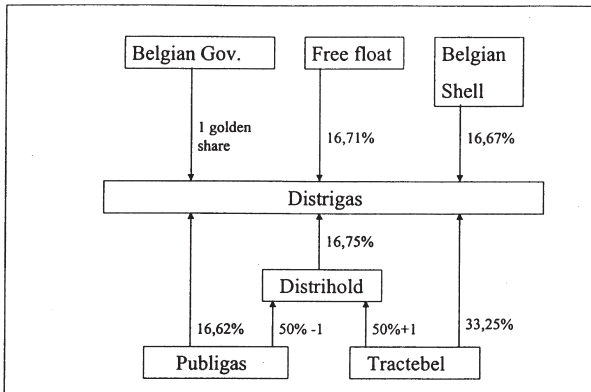


Fig. 3. Privatisation of Distrigas (spring 1994).

In September 1996, the Belgian financier Frère sold his 24.5% minority stake in Tractebel to SGB and used the cash he obtained to buy a share in Suez. Accordingly, SGB increased its share in Tractebel from 40.5 to 65%. The announcement in March 1997 of the merger between Suez and Lyonnaise des Eaux, another French utility holding, again provoked uncertainty at the Tractebel headquarters since Lyonnaise des Eaux operates in the same markets. Tractebel reacted by merging with its subsidiary Powerfin in May 1997. Consequently, SGB's stake dropped from 65% to 50.3%. Tractebel's stake in Electrabel went down to 39.9%. The other Electrabel shareholders are the MIU (5.01%) and the banking group Fortis AG (1.93%). Tractebel and the Belgian government also asked for structural guarantees and a system of "corporate governance" for Tractebel.

In mid June 1997 the general meetings of both groups, Suez and Lyonnaise des Eaux, approved the Suez–Lyonnaise des Eaux merger. Some days later, on 20 June 1997, an extraordinary general meeting approved a modification of Tractebel's articles of association. The new articles are unique in Belgium, going much further than foreseen by the Belgian company law rules relating to conflicts of interests at the board of directors. They distinguish three types of managers: those representing the controlling shareholder, the independent managers and those representing the other shareholders. The independent managers embodying the independent strategic committee are forbidden to exercise any function at the level of the group Suez–Lyonnaise des Eaux, SGB or Tractebel and to represent a shareholder holding more than 3% of the total capital or 5% of a company being the shareholder of a Tractebel shareholder. If conflicts of interests exist, the independent managers have to notify it to the board. If the board is unable to reach unanimity, the managers representing the controlling shareholders are prohibited from voting on this issue (Fig. 4).

Since April 1998 the group Suez–Lyonnaise des Eaux (the Group) has been eager to strengthen its economic interests in Tractebel in which it holds the majority of the shares through its 63.4% holdship in SGB. The group expressed its desire to acquire 100% of the SGB capital via a public exchange offer. At the beginning of August it proudly presented to have 99.4% of the SGB shares. At the end of February 1999, the strategic committee advised the Tractebel board of directors to appoint Jean-Pierre Hansen, Electrabel's CEO, as CEO of Tractebel. The board of directors confirmed the advice on 18 March 1999. This evolution proves that the unique "corporate governance" device is not working properly at the moment that Mr. Bodson, the symbol of limited autonomous development, had to resign under pressure from the Group. More subtle and more important are the underlying choices taken by two key players, Etienne Davignon, the SGB president and Albert Frère, who currently holds an 11% stake in the group, making him its biggest shareholder, for serving and co-operating with the group.

For several years a possible merger between the

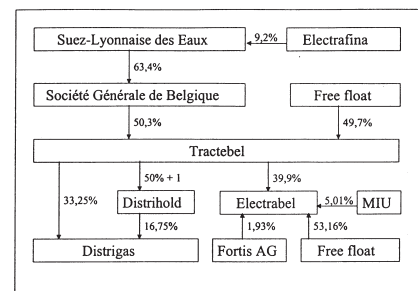


Fig. 4. Control structure of the Belgian energy sector (June 1997).

activities of Tractebel, Electrabel and Distrigas has been in the pipeline. Contrary to the Group's fear of a drop of its ownership below 50% in case of a merger, the Tractebel former CEO Mr. Bodson has always been favourable to this idea. So far the Group has blocked the merger plans. This trend may ultimately lead to the creation of a single electricity and gas company when Tractebel, Electrabel and Distrigas merge. The restructuring, however, is likely to create new entities or reshuffle activities among and within the existing companies e.g. to organise participations in the electricity and gas markets abroad. At the end of February the Group decided to make Tractebel its exclusive development pool in the energy field. In this regard SGB took over Elyo, the 100% French energy subsidiary of the Group, at the end of March 1999. Later Elyo will be integrated into the Tractebel holding. On 23 April the newspapers reported the plan to transfer the most important assets of Tractebel and Distrigas to Electrabel. The underlying idea is to organise the Belgian electricity pool without having to proceed to a legal merger of the existing companies.

The most recent episode in the Belgian energy sector story dates from August 19 when the Group launched a bid on the remaining 49% shares of Tractebel. In early November they announced the acquisition of 96%. As a result, the Group also obtains the control of Electrabel and Distrigas. The question now arises as to whether and when the latter companies will merge into one company (Fig. 5).

2.4. Amalgamating instead of unbundling electricity sector functions during the 1995 restructuring

In May 1988 the European Commission presented its White Paper on the Internal Energy Market. At that time Belgium had three small private generators Ebes, Intercom and Unerg, several smaller public generators united

in SPE, and a small gas company Distrigas. Save for the Netherlands having four small-scale generators, the neighbouring power companies like RWE in Germany and EDF in France were much bigger. Accordingly, the Belgian power sector underwent changes. The three private producers Ebes, Intercom and Unerg merged into one company Electrabel. Likewise, a decade earlier the smaller public electricity generators in a few cities were united in one entity called SPE (1978), as they were not able to reach the minimum efficient scale. In 1981 SPE joined the three private companies in organising a modern central dispatch system for merit order loading of all their plant, as well as a unified system for investment planning, tariffs, general policy, central dispatch of the power system, grid investments and maintenance, research, nuclear issues and fossil fuel transactions.

In September 1990 a protocol confirmed the 1981 cooperative agreement between the private power companies (now Electrabel) and the public generator SPE. In January 1995 a "quasi merger" of Electrabel and SPE came about. The merger has undoubtedly fenced the Belgian electricity market from other companies. Electrabel-SPE currently generates jointly 96% of the Belgian electricity and is involved in the construction of new generating capacity. Moreover, the remaining decentralised capacity is either partly or completely owned by Electrabel and SPE on the basis of partnerships.

The central position in the new electricity sector structure envisaged by the January 1995 convention between Electrabel and SPE is the "Participative Association", a non-incorporated body. The association has no societal goals but is limited to the object of handling power and money. The real centre of operation of the electricity system is the 1995 restructured Co-ordination of Production and Transport of Electricity (CPTE) (Verbruggen et al., 2000). The new CPTE encompasses the previous subsidiaries of Electrabel and SPE, the "participative organisation" Gecoli and the previous limited company CPTE. Electrabel holds 91.5% of CPTE's shares, SPE the remaining 8.5%. Prior to the reform, CPTE owned the national dispatching centre in Linkebeek and was responsible for the central dispatching of power plants and electricity flows over the transmission network. Gecoli owned the transmission network of 380, 220 and 150 kV and was accountable for maintaining and performing the network.

As agreed in the convention establishing the "quasi-merger", Electrabel and SPE have given their production plants and transport network in property and in usufruct to the new CPTE. However, the management of the power plants was conferred upon Electrabel and SPE, the management of the transport network upon Electrabel only. The new CPTE performs the activities of the previous CPTE and Gecoli. The new CPTE consists of six technical committees dealing with issues such as

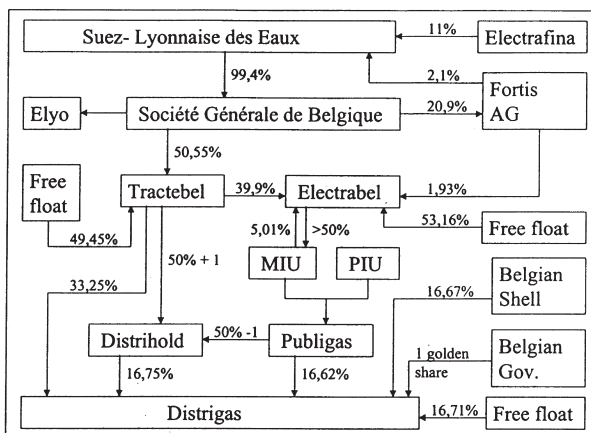


Fig. 5. Control structure of the Belgian energy sector (March 1999).

planning and co-ordination, fossil fuels, nuclear energy, conventional generation and environment. Next to the new CPTE, the Board of Electricity Companies (BCEO–CGEE) operates, which deals with the Control Committee (CCEG) and with public authorities mainly about investment planning, tariffs and accounting. This new structure emerging from the 1995 convention has reduced the level of competition in the Belgian bulk power supply market to an absolute minimum. However, seen in its relevant market, the European Union, the concentration is of minor importance.

### 2.5. *Electrabel consolidates its control on the distribution/retail supply activities in 1996*

In November 1995 Intermixt and Electrabel worked out a plan to consolidate Electrabel's monopoly position in the Mixed Intermunicipal Utilities (MIU). The plan consisted of the premature renewal of the existing contracts. These contracts were incorporated in the second-generation articles of association of the MIU. These articles normally expire between 1998 and 2022. The approaching liberalisation of the European energy market urged Electrabel to speed up the renewal of the existing contracts.

In spring 1996 new contracts (Verbruggen, 1996) for the mixed intermunicipal utilities were agreed upon by Electrabel and the municipal boards. The main issues covered by these new contracts, also known as the third generation articles of association, are as follows. Electrabel has the exclusive right of delivering power to the MIU. Also, if the MIU wants to install generation capacity, it can do so only by giving the order to Electrabel. Taxes may be levied upon direct clients of Electrabel, independent producers and industrial customers buying power from a producer other than Electrabel. Laws may impose a tax levy on autoproducers. Experts may be assigned to the municipal representatives in the MIU. Municipalities could only obtain a maximum of 50% of the MIU's share capital. Municipalities were offered the possibility to subscribe to Electrabel shares amounting to 5.01% of the share capital. These shares are temporarily administered by pure financing intermunicipal utilities bearing no influence upon the policy of the MIU.

The European Commission opposed these new contracts claiming that they contravened articles 85 and 86 on competition<sup>4</sup> law of the EC Treaty. The Commission strongly objected to the protection of the domestic market against other producers and/or suppliers, to the 18 year-term of the contracts and the participation of the municipalities in Electrabel's share capital. After negoti-

ations the Commission and Electrabel finally reached an agreement in April 1997. The Commission accepted the 15-year contract term proposed by Electrabel. After 10 years, in 2006, other producers can supply 25% of the electricity demand of the MIU. Until 2011 Electrabel will deliver the remaining 75%. The 5% participation will come to an end when the third generation contracts expire.

Through its successful move Electrabel will prolong its dominant position in the different parts of the Belgian electricity sector in the next millennium. The events which occurred in 1996 undoubtedly confirm the willingness of Electrabel to prepare for European competition. It also proves that the European Commission has the authority to prevent anticompetitive practices. Unfortunately, the 1996 movements also confirm the strategic, political and organisational strength of Electrabel in the Belgian market and the weakness of public authorities and regulatory control in this country. This strength is based on contract, property and company law, and on a firm commitment to a stringent strategy of preserving monopolistic power.

## 3. The new Act concerning the organisation of the electricity market

### 3.1. *Preparing for implementing EU-directive 96/92 in Belgium*

On 19 December 1996, EU-directive 96/92<sup>5</sup> concerning common rules for the internal market in electricity was adopted. The member states were required to implement the directive by 19 February 1999. Belgium<sup>6</sup> was allowed to postpone the implementation for 1 year. In June 1998 the responsible Minister Di Rupo prepared a draft policy note (Di Rupo, 1998) of poor quality. It did not reach the level of discussion, and in July 1998 energy as a competency was conferred upon the Minister of Defence Poncelet. He published a new policy paper (Poncelet, 1998) in October 1998.

In the weeks following, the note was approved by the Council of Ministers and commented on by the regions. By the end of November the note was converted into the first draft bill concerning the organisation of the electricity market. The second draft bill of 3 December slightly refined the first bill with regard to the structure of the regulator. On 18 December the second draft bill was approved by the Council of Ministers after the Interministerial Conference on Economics and Energy of 9

<sup>4</sup> Article 12 of the Treaty of Amsterdam came into force on 1 May 1999 and provides for the renumbering of the EC Treaty articles. Articles 81 and 82 replace articles 85 and 86.

<sup>5</sup> Anon. (1997). For a comment, see Geneste (1997) and Hancher (1997). See also Verbruggen (1997).

<sup>6</sup> Verbruggen and Verheyen (1997); for a comparative study between the Dutch and Belgian Electricity Act, read Verbruggen and Vanderstappen (1999).

December. A few weeks later on 19 January 1999 the bill was submitted to the Chamber of Representatives.

The bill was then discussed for several weeks in the Commission for Economic Affairs. Despite the 37 amendments of the opposition, the Commission for Economic Affairs nevertheless approved the bill majority<sup>7</sup> against minority on 24 February neglecting all the amendments made by the opposition while adopting the additional 6 minor amendments of the government. On 11 March the amended electricity bill was adopted by the plenary Chamber of Representatives and sent to the Senate. Similar to the Chamber of the Senate, the Commission of Economic Affairs discarded all 41 of the opposition amendments on 20 April and, consequently, the plenary Senate decided two days later that there was no reason for amending the electricity bill. Finally, the Act concerning the organisation of the electricity market was adopted<sup>8</sup> on April 29 (hereinafter the 1999 Electricity Act).

It was a common practice of the former<sup>9</sup> government to decide upon important issues in a short time without ample consultation of the parties involved. The overall process consisted of delaying important legislation until the end of the legislative period when they were then speeded up. Similarly, we have noticed several times this type of urgency<sup>10</sup> in the Belgian energy sector, avoiding every meaningful discussion and leaving all discretionary power to the incumbent interests of Tractebel and Electrabel. The fact that the additional year to implement EU-directive 96/92 was not used is owed to the principle of reciprocity. According to this principle, generators can be barred from entering a foreign market where there is a higher level of market opening compared to the national, domestic market of the generators. This could mean that, pending the adoption of the Belgian Electricity Act, other member states would prohibit the entrance of Electrabel into their market. Moreover, the Electricity Act 1999 establishes a platform of market operation in the bulk market. However, the main problem concerns the fairly empty domestic market because of the very high threshold for network access, i.e. an annual consumption of 100 GWh. The main issues of the Act are broadly discussed below.

<sup>7</sup> At that time the christian democrats and socialists had the majority in the federal parliament.

<sup>8</sup> Anon. (1999a); the same day the new Belgian Act concerning the organisation of the gas market was published.

<sup>9</sup> The liberals and the greens won the elections of 13 June 1999 and formed a tripartite government with the socialists. The former government was composed of christian democrats and socialists.

<sup>10</sup> This is illustrated by the request of former Minister Poncelet to the department legislation of the Belgian State Council on 21 December to give urgent advise on the bill within the extremely short time-period of only three days.

### 3.2. Regulation

The Commission for Regulation of Electricity and Gas (CREG) will be charged with the advisory task vis-à-vis the authorities regarding the organisation and operation of the electricity and gas market. It also supervises and controls the application of the electricity and gas laws and their executive orders. CREG is responsible for the eligible market. The CCEG continues to control the non-eligible or captive market. The CREG consists of a Management Board and a General Council. The Management Board is responsible for taking the measures necessary to perform the tasks entrusted to the CREG. It is composed of a chairman and five members each heading a section. The six sections encompass market disputes, technical operation of the electricity and gas market, control over prices and accounts on the electricity and gas market, administration and finance. The General Council supervises the Management Board. The former determines guidelines for the application of the laws and orders, evaluates the tasks performed by the Management Committee and supervises the co-ordination of the activities of CREG and CCEG.

The CREG may request the electricity undertakings on the Belgian market to provide all relevant information and may control their accounts on the spot. The CREG establishes a conciliation and arbitration service to settle disputes in the electricity sector concerning transmission network access, application of the grid code and tariffs for regulated access. By Royal Order the transmission network operator can be obliged to be subjected to this service. At the CREG an "Appeal Chamber" decide upon pre-contractual disputes between the network operator and the network users relating to transmission network access. Its competence is limited to pre-contractual disputes. This chamber takes administrative decisions. To ensure compliance, the CREG is competent to impose administrative fines. Disputes about contractual rights have to be brought before the courts. Compliance with the 1991 Competition Act continues to be the prerogative of the competition bodies. A Royal Order will ensure co-operation between them and the CREG.

The General Council is a clone of the CCEG (see Fig. 6). It comprises<sup>11</sup> representatives of the federal government, employers (FBE), employees (trade unions) and SME organisations, generators, distribution companies (Intermixt and Inter-Regies) and consumers. The regional governments are also invited to send representatives. However, contrary to the composition of the CCEG, the CREG constitutes a larger platform as it expressly includes representatives of SME and con-

<sup>11</sup> The detailed composition of the CREG is dealt with by Royal Order of 3 May (Anon., 1999b).



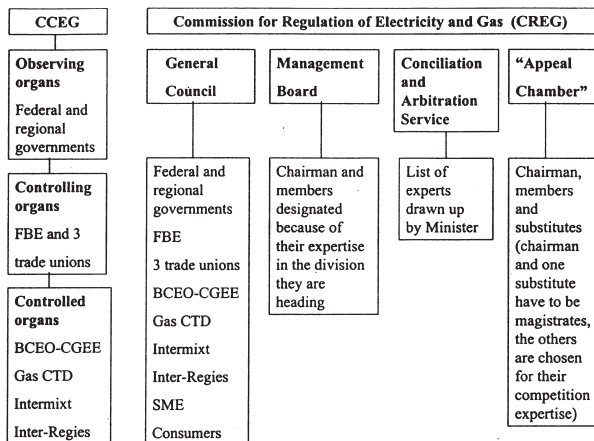


Fig. 6. Composition of the CCEG and CREG.

sumers. Unfortunately, environmental organisations are not invited to take a seat in the General Council.

Our comments relating to the composition of the CREG can be summarised as follows. The splitting of the CREG into a Management Board and a General Council is the wrong approach. Three entities (CCEG, the General Council and Management Board within the CREG) are involved in regulation, putting the Management Board in a subordinate position. The General Council supervises the Management Board. The establishment of the General Council will seriously hinder the functioning of the CREG as an independent and specialised regulator. The presence of the power generators within the Council supervising the Committee, that in its turn controls the generators, confirms their self-controlling role as in the CCEG. So, power generators are controller and controlled at the same time. Accordingly, the CREG should be restricted to the Management Board<sup>12</sup>.

Moreover, it is to be regretted that the competencies and responsibilities of the CCEG<sup>13</sup> and CREG, exclusive of the General Council, are not clearly drawn up and tuned. The CCEG and CREG will, for instance, cooperate to verify the absence of cross-subsidisation between categories of consumers. However, the Act does not stipulate which of the organs holds the final decision-making power. For reasons of transparency, efficient control and good regulation it is to be preferred to have one single regulator, the CREG. It is also to be regretted that the 1999 Electricity Act does not mention any form of agreement with the regions for establishing one collective regulatory body of the electricity sector, distribution of electricity included.

For reasons of democratic control it would be better

to construe the CREG as an agent of legislative power. The agent should receive guidelines from and be controlled by the legislative power. He should also submit an annual report. The regulating and controlling functions of the CREG should be restricted to the Management Board. The authority of the General Council being to a large extent a face-lift of the CCEG, the "captured regulator", goes back to the post-war period when the employers' federation and trade unions were favouring an "economy of deliberation" over nationalisation of the electricity supply industry. Besides, the government being the "agent" of the legislative power merely performs an observing role.

### 3.3. Independent network operator

The operation of the transmission network is taken care of by one network operator, who is also responsible for ensuring the maintenance and development of the transmission network in a given area and its interconnections with other networks in order to guarantee security of supply. The operation of the distribution network is a regional competence requiring implementation by decree. The transmission network operator must be established in the form of a private company, being a separate legal entity. It must refrain from electricity generating and supplying activities except for accessory activities necessary to guarantee the technical maintenance. In addition, it may not have direct or indirect stakes in generators, distributors or agents.

The government determines more precise provisions to ensure the operator's independence. These provisions deal with the composition and operation of the management organs, "corporate governance" rules, the financial independence of the personnel, the insurance of confidentiality of commercial data regarding network users and the prevention from any discrimination between (categories of) network users in favour of associated companies.

The Royal Order of 3 May concerning the administration of the national transmission network for electricity (Anon., 1999c) designed several "corporate governance" mechanisms. They relate to the presence of non-executive<sup>14</sup> and independent directors at the board of directors, and the creation of a corporate governance committee, audit committee, remuneration committee and management committee. In particular, the corporate governance committee will propose the independent directors and, even more important, investigate each conflict of interests between the network operator on the

<sup>12</sup> See amendment No. 5 of the MP's Van Dienderen and Deleuze.

<sup>13</sup> In amendments Nos 20 to 23 MP De Grauwe even argued to abolish the CCEG as the regulator for the "captured market".

<sup>14</sup> They may not be a director of the network operator or of one of its subsidiaries.

one hand and a dominating<sup>15</sup> shareholder or an undertaking associated or connected with a dominating shareholder on the other hand. For reasons of democratic participation we believe these essential aspects would have been better undertaken by statutory provision or by an ordinary act<sup>16</sup> of the federal parliament.

The Minister entrusted with energy matters designates the network operator proposed by the network owners possessing individually or globally a part of the system covering at least 75% of the national territory and two thirds of the territory of each region. In practice, this cannot be anyone but the CPTÉ of Electrabel–SPE. The designation lasts for an extendable time-period of 20 years. The government also draws up the grid code as well as the overall structure of the tariffs for interconnection. The tariffs are determined in accordance with basic principles like non-discrimination, transparency, unbundling, cost accounting, and reasonable remuneration for network investment, geographical uniformity. The transmission network operator also designs a plan for developing the network and its personnel is bound by professional secrecy.

There exists a general consensus that control over the transmission network by owners of generation assets provides a serious impediment to the development of a competitive electricity market (Della Valle, 1997). The concern is that owners of generation assets may be able to influence generation prices by determining the way the transmission system is used, operated, maintained or expanded. Most parties in the electricity restructuring process are convinced by the idea that one needs to separate or “unbundle” transmission from generation assets. The question then is how this should be accomplished. Belgium has opted for operational unbundling by means of an independent network operator (ISO). By placing all operational responsibilities in the hands of an ISO, the power generators do not need to unbundle their transmission assets on a functional level (separating generation and transmission functions into two distinct organisations within the same corporation) or corporate level (divesting all generating assets).

Although the Royal Order of 3 May enumerates various “corporate governance” provisions by the government to take measures guaranteeing the operator’s independence, one may doubt its true independence in practise, and effective control over the system. To ensure more independence, we have advocated handing over the entire share capital<sup>17</sup> of the transmission network operator to the state, i.e. the federal and the three regional

governments. Prior to 1995 the balance between generators and the network was efficiently administered by the pre-CPTÉ. Therefore, operation of the network might have been easily attributed to the pre-1995 CPTÉ, pre-scinded from the Electrabel–SPE construction. Besides, if one intends to implement the “spirit” of Directive 96/92 and to create a transparent and efficient ISO one should have isolated the maintenance and development of the network from the actual CPTÉ and again have conferred these functions upon the pre-1995 Gecoli. With regard to the calculation of transmission tariffs we regret that standards of efficiency and benchmarking are not embedded in the Electricity Act.

### *3.4. Generation planning, investment and licensing for constructing new plants*

An indicative program for power generation replaces the national investment plan. Accordingly, the National Committee on Energy will be dissolved. In collaboration with the Administration for Energy the CREG will draw up this program having no binding character. We consider it wrong to entrust the CREG with an estimation of the evolution of the electricity demand and the corresponding need for means of production. Save for the creation of the CREG, governmental interference must be limited to a minimum. The equilibrium between electricity demand and offer of production means should be realised by the market. Therefore, governmental intervention through this indicative program endangers the normal functioning of the market.

For the construction of new generating capacity, Belgium has opted for an authorisation procedure. A Royal Order will lay down criteria for the grant of constructing licences. These relate in particular to the safety and security of the electricity system, installations and associated equipment, energy efficiency, the nature of primary sources, characteristics of the applicant such as technical, economic and financial capabilities. The federal minister for energy grants the individual licence, but the regional authorities may impose licences relating to their competencies in environmental protection and spatial planning. By generally stating that the construction of new power plants is subjected to a federal licence, the Act de facto infringes the competency of the regions on the grant of licences for generating capacity based on rational use of energy or renewable energy sources.

In order to streamline procedures for obtaining licences, agreements of co-operation between the state and the regions will be concluded. Moreover, a new legal framework has been created for assigning domain concessions for gaining electricity via water, river flows or wind in maritime areas. In this regard one thinks of constructing offshore wind plants. The construction of new direct lines, not forming part of the distribution network, is also subjected to a ministerial licence. The granting

<sup>15</sup> Every natural or legal person and every group of persons adhering to the same line of action, who directly or indirectly own at least 10% of the operator’s capital or of the voting rights attached to the shares issued.

<sup>16</sup> Amendment No. 26 of the MP’s Clerfayt and Hotermans.

<sup>17</sup> Like the Swedish Svenska Kräftnet; Petsala (1995).

may be made dependent on the refusal of network access. Again, the Act implicitly erodes regional competence by not defining the level of voltage of the direct lines.

### 3.5. Network access and eligibility

The basic formula used for transmission network access is the system of regulated third party access. Suppliers and eligible customers have a right of access on the basis of published tariffs for use of the network. Access can be denied on grounds of insufficient capacity and non-compliance with the criteria laid down in the network code. However, the Act also states that the formula of negotiated access remains applicable to cross-border transport. Moreover, a Royal Order may apply the latter formula to certain categories of transactions implying huge quantities. We argue that one should stick to one<sup>18</sup> system of network access: either negotiated or regulated access. Regulated access is to be preferred assuming that it is accompanied by good regulation. A mixture of two systems inevitably brings about discrimination and cross-subsidisation between categories of consumers.

The definition of eligible consumer is limited to final<sup>19</sup> consumers consuming more than 100 GWh per year on a consumption site basis and including autoproduction according to criteria established by Royal Order. However, the notion consumption site is not defined so that it may apply to undertakings forming part of the same industrial group or consumers forming a consortium or living in the same industrial area. This interpretation is compatible with the opinion of the European Commission allowing cumulative calculation. In this regard we regret the lack of the notion consumption site in the electricity bill itself.

Since these big industrial customers represent about 33% of the electricity consumption, the initial market opening of 26.48% required by EU-directive 96/92 is largely exceeded. The government is authorised to lower the eligibility threshold to final consumers connected to the transmission network in order to ensure their entire eligibility eventually by the end of December 2006.

Similarly, the distribution companies are not eligible before 2007, save for the volume of electricity consumed by the final consumers designated as eligible within their

distribution network in order to supply those customers. However, the extent of their freedom of choice depends on their contractual obligations vis-à-vis Electrabel. The regions may however advance their eligibility by declaring their final consumer within the distribution network to be eligible. To avoid that, generators seated in other member states with a lower level of market opening than the Belgians are given a “free ride”, the principle of reciprocity has been integrated.

Distribution companies have to be regarded as eligible consumers. In other EU member states, except for France and Italy where there are big national public generators, distribution companies are already eligible. Even though the issue in the Belgian electricity sector is more complicated as the municipalities get about 8% of their revenues out of electricity distribution and also hold 5% of the Electrabel shares, it seems difficult to defend a legal discrimination between different types of consumers having a comparable level of consumption, like eligible industrial consumers and distribution companies.

Distribution companies should also be treated the same as other final consumers in order to reduce cross-subsidisation. Electrabel maintains its competitive position by charging low tariffs to large industrial consumers, while maintaining high tariffs for small consumers and SMEs. In 1996 Electrabel (Electrabel, 1997) realised a gross profit of 37.6 billion Belgian francs (BEF) of which 94% (35.4 billion BEF) came out of the MIU. Sales through the MIU represent 60% of the electricity supply sale. 1 kWh sold through a MIU provides approximately a net profit amounting to ten times the net profit resulting from a direct sale to large consumers<sup>20</sup>. Because of the more irregular demand pattern of non-industrial consumption, it is normal that non-industrial prices contain a larger mark-up above costs than industrial ones, but the difference applied in Belgium is excessive<sup>21</sup>.

If the distribution companies or small consumers are not directly eligible, the small consumers and SMCs will probably be “captured” for a long while in an electricity supply industry having tariffs belonging to the higher<sup>22</sup> ones in Europe. The 1000 kW threshold in the 1925 Act could be used for defining eligibility. It does not require institutional changes, and distribution companies are

<sup>18</sup> See amendment No. 2 of the green MP's Van Dienderen and Deleuze and amendment No. 15 of the liberal democratic MP's Van den Abeelen, Lano and De Grauwe.

<sup>19</sup> In amendment No. 17 the MP De Grauwe suggested replacing “final consumer” by “consumer”, so that distribution companies are included. Simultaneously, the threshold of 100 GWh annual consumption is to be replaced by 1 GWh. In amendment No. 3 the MP's Van Dienderen and Deleuze also advocate the inclusion of the distribution companies.

<sup>20</sup> From a business economics point of view these figures are not the best figures to analyse Electrabel's business costs and profits. In order to have a more accurate view on the profit account, one needs to have at one's disposal the analytical book-keeping. However, these data are not available.

<sup>21</sup> In his Ph.D. Thesis (De Braeckeleer, 1990) F. De Braeckeleer tried to find out whether the prices applied to bulk and domestic customers obeyed the Ramsey-pricing rules. By lack of access to reliable supply cost data, the study could not provide clear evidence on the issue.

<sup>22</sup> While tariffs charged for large industrial consumers are reckoned to be one of the cheaper in the European Union.

automatically included. Later on then, the non-eligible or “captured consumers” can have free choice in a phased<sup>23</sup> way, starting with consumers above 100 kW.

### 3.6. Price regulation, unbundling, public service obligations and stranded costs

On recommendation of the CCEG, the federal minister for economic affairs determines the maximum prices for supplying electricity to non-eligible consumers. He can also set maximum prices, on recommendation of the regulator, for supply of electricity to eligible consumers. Prices are composed of costs of service and a rate of return. The 1999 Electricity Act vindicates price caps on three grounds: to avoid cross-subsidisation, to make sure that non-eligible consumers receive a reasonable share of the productivity improvement due to liberalisation and to tune prices to those applied in the same market segment in other EU member states, taking into account the special characteristics of the distribution sector. After consultation with the regional governments, the federal government may lay down minimum prices for the purchase of co-generated power for supplying non-eligible consumers.

The transition to an open and liberalised electricity supply industry justifies the imposition of public service obligations. In this regard the Act empowers the government to impose obligations relating to regularity and quality of supply and the supply of non-eligible consumers. It may also create a fund, monitored by the regulator, to cover fully or partly the real net cost of the public service obligations and the stranded costs. The fund will be fully or partly financed by extra charges on network tariffs or by levies imposed on all or certain categories of consumers. The order regulating the financing of this fund needs to be confirmed within six months by statutory instrument.

Public service obligations will be a necessary measure in Belgium because of the long tradition of trade union commitment, as for instance the social tariffs. We do not think that public service obligations money should be reserved for continuing the system of national uniform tariffs. All categories of final consumers should be required to contribute to the fund since extra charges on network tariffs might hinder competition between market participants. In the bulk market of electricity we find it difficult to imagine any public service obligations requiring the establishment of a special fund. On the contrary, in the retail market the public service obligations encompass social obligations, such as the obligation to be connected, the minimum supply for small

consumers, special tariff for special consumers, and environmental obligations, such as promotion of rational use of energy on the energy-demand side and promotion of renewable energy sources and energy efficient generation at the energy-supply side. In the bulk market they merely seem to be disguised stranded costs. Although stranded costs should be restricted to the initial construction of the nuclear sector in the 80s and not to cover the costs relating to retirement of personnel, it is finally up to the European Commission to decide what is to be understood by stranded costs.

Every undertaking, irrespective of its legal form, involved in the electricity industry has to comply with the provisions of the 1975 Accounting Act. Unbundling of ESI functions is limited to accounting. The CREG is empowered to control the accounts on the spot. Vertically or horizontally integrated undertakings are bound to keep in their internal accounting separate accounts for their generation, transmission and distribution activities, and where appropriate, consolidated accounts for non-electricity activities as if they were carried out by separate undertakings. The explanation in the annual account should also mention significant transactions with allied and associated undertakings. CREG may request the electricity undertakings to transmit periodically the figures and descriptive data concerning their financial and commercial relations with allied or associated undertakings to enable CREG to investigate whether those relations do not harm the essential interests of the consumers or the good performance of public service obligations.

In addition, electricity companies having a strong position on the Belgian electricity market, i.e. a market share of more than 25% of the electricity market or a segment, should integrate in their internal decision-making process appropriate mechanisms to avoid conflicts of interest by allied or associated undertakings leading to the adoption of decisions or strategies that might harm these latter interests and obligations. The aim is to ensure appropriate objectivity of management in groups of companies and respect of the “at arm’s length principle” in intra-group transactions. In this regard, CREG makes non-binding recommendations inspired by the rules of “corporate governance”. Companies have to explain their motives for derogating to those rules.

## 4. Conclusion

In conclusion, the 1999 Electricity Act is confined to establishing a legal framework necessitating implementation by Royal Executive Orders. These abundant delegations jeopardise democratic control. Belgium needs another system of public intervention with regard to public service obligations. The regulator CREG should be the agent of the Parliament. An increase of governmental

<sup>23</sup> Starting immediately with consumers above 1000 kW and from spring 2003 onwards consumers above 100 kW. By the end of 2003 all consumers. See also in this regard amendment No. 18 of MP De Grauwe.

or royal powers should be balanced by a fortification of parliamentary control on regulation. Important issues must be precisely defined and dealt with by statutory instruments. Important delegations to the government, such as the creation, operation and independence of the transmission network operator, should a posteriori be confirmed by statutory instruments.

The Act also neglects the competencies of the regions. They are deemed to play an ancillary role. Co-operation with the regions in overlapping matters should be intensified. Accordingly, the Belgian electricity market will be opened formally. A true opening requires a much more independent transmission network operator, an efficient and quick-witted regulator and free access for suppliers and consumers. In this regard one has to await the first steps of the new liberal–socialist–green government installing in early September the creation of a group of experts entrusted with the investigation of these issues.

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